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# MORTGAGE BANKING

FEBRUARY 1990

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COVER ILLUSTRATION BY REBECCA LEER

# A Cause for Celebration?

Automation is clearly a critical component of any mortgage operation. The benefits of automation are being felt on both the production and servicing fronts. Stark evidence that automation is paying its way on the servicing side emerges from the industry cost study just released by the Mortgage Bankers Association.

Two convincing signs of higher productivity during 1988 in the servicing operation will warm the heart of the industry's managers. The average number of loans serviced per servicing employee jumped by 46 loans in one year's time. In 1987, that average was only 570 loans. But in 1988, the average per servicing employee rose to 616 loans. This is the highest level of productivity since 1981, notes MBA's economics department—the authors of the study. The study profiled the top 10 most profitable firms amongst the respondents. This group posted on average 703 loans per servicing employee and boasted total direct costs that averaged 26 percent less than the other firms responding.

The other notable trend on the cost side was the finding that servicing personnel expenses dropped for the first time since 1984 on a per loan basis. Personnel expenses represent about 40 percent of the direct expenses tied to servicing. As one of the major controllable cost items in the servicing management equation these expenses are critical and obviously can make or break servicing profitability. On a per loan basis, personnel costs dropped by a full 8 percent in 1988 compared with 1987's figures.

The average cost of servicing a loan in 1988, accounting for direct expenses only, totaled $87.55. Personnel expenses per loan accounted for $37.63 of those costs in 1988, down from $40.84 in 1987.

Is this enough? Should servicing managers rest on their laurels and proclaim victory? Unfortunately that is not in the cards since foreclosure and delinquency problems continue to wage war on servicing profitability. In 1988, total expenses for problem loans were 11 percent higher than in 1987. Yet, even with the profit drain tied to bad loans, the final tally for 1988 showed that net income per loan serviced rose to $49.36—a rise of almost 32 percent over 1987's dismal showing. Not bad, but let's wait for 1989's numbers before we buy the confetti.

Janet Reilley Hewitt
Editor

## COMING IN MARCH

A whirlwind of reform is clouding the housing legislative outlook. Lawmakers in Washington are bent on a mission to scrutinize all government-related housing programs and tighten as many screws as they can—loose or otherwise. Next month we will talk about what's ahead and what's already been done on the housing legislative front.

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Offsetting otherwise gloomy profitability results, MBA's cost study showed net income from servicing in 1988 rose 32 percent for the average reporting firm.

# THE 1988 SERVICING PROFIT PICTURE

Robert M. Rosenblatt

Profitability in mortgage lending in 1988 was little better than in 1987, as the industry continued its efforts to cope with difficult environmental conditions. Loan origination volume remained deeply depressed during 1988, and the costs of handling delinquent and foreclosed loans were once again exceptionally high. Rising short-term interest rates, which increased the costs of carrying mortgages in warehouse, added to the problems of maintaining profitability.

For the 114 mortgage banking firms that provided detailed 1988 statistics on income and costs by mortgage banking function, the average pretax profit margin (net income per dollar of gross revenue) was 1.7 percent in 1988, barely above the meager 1987 level. Profit margins were increased to 14.3 percent by sales of servicing, but of course this entails a sacrifice of future income to bolster current profitability. (See Table 1)

Sustaining profitability was as difficult for larger firms as for smaller companies. Thus, profit margins at firms originating more than $500 million in loans were slightly negative, as they were also at firms originating less than $100 million in loans. While companies originating from $100 million to $500 million in loans were somewhat more profitable, the variations in profitability among firms within these size groups is too large for this result to be significant.

Gloomy as these results are, the aggregate data on profitability in single-family residential lending during 1988 contain some elements of hope. For one thing, net income from servicing at the average reporting firm rose 32 percent from a very depressed level in 1987. Successful efforts to control direct servicing costs were a major contributor to this improvement. Second, some firms demonstrated once again that good levels of profitability can be sustained even in a harsh environment. For example, of the firms reporting in both the 1987 and 1988 surveys of income and expenses, the 10 most profitable achieved an average profit margin of about 15 percent in both years. This is below the industry-wide average for good years such as 1986, but is very close to the industry-wide average for the past decade.

After suffering through two extremely difficult years, profitability from the servicing operation improved in 1988. While mortgage bankers still have a long way to go to regain satisfactory levels of profitability in servicing, information from this survey indicates that many firms are learning to cope with the difficulties they face in a highly competitive business environment.

Net income per loan serviced rose to $49.36 in 1988, from $37.49 in 1987, an increase of nearly 32 percent. One contributor to this improvement was the continued increase in gross income. Total servicing income, at $211.44 per loan, was 8 percent higher in 1988 than in 1987. But the main reason for this progress was the stability in total servicing costs. In 1988, total costs rose only 2 percent to $162.08 per loan. In sharp contrast, servicing costs per loan had jumped 18 percent

After suffering through two extremely difficult years, profitability from the servicing operation improved in 1988.

in the previous year. The key to holding down overall expenses was the 10 percent drop in direct costs to $87.55 per loan, reflecting an increase in productivity. The number of loans serviced per servicing employee rose from 570 loans in 1987 to 616 loans in 1988, or by 46 loans per employee. This is the highest level of productivity since 1981. Moreover, in 1988, 17 percent of the firms in the survey serviced at least 700 loans per servicing employee. In 1987, only 11 percent of the sample achieved this level of productivity.

The 1988 rise in profitability in servicing was the first in four years. In 1988, the profit margin (net income divided by gross income) for the servicing operation increased by 4 percentage points to 23 percent. Nonetheless, profitability is still quite low by historical standards. As recently as 1985, the profit margin for servicing was 42 percent, and for the period 1980-1985, the profit margin averaged 49 percent per year. A major reason for the deterioration recently has been the heavy losses associated with delinquency and foreclosure problems. Total servicing expenses related to problem loans rose again in 1988, this time by 11 percent, to $37.42 per loan. (See Table 2)

### Servicing Income

Total servicing income rose by 8 percent to $211.44 per loan in 1988 as compared with $195.81 per loan in the previous year. As a result, servicing income as a percent of the dollar volume serviced rose to 45 basis points, 2 basis points higher than in 1987, and equal to the average for the 1980s. Within servicing income, servicing fee income, the most stable and important part of most servicing operations, rose 3.4 percent to $183.60 per loan, while other loan administration income increased by 28 percent to $29.80 per loan. Furthermore, losses on sales of real estate owned (REO) were only ($1.96) per loan in 1988 as compared with ($5.08) per loan in 1987, an improvement of $3.12 per loan. However provision for loan losses, an element of costs, rose significantly in 1988.

In addition to the traditional sources of revenue generation previously mentioned, a broader understanding of the growth of servicing income today requires taking into account the buying and selling of servicing rights, a practice that has become more prevalent in recent years. Estimates reveal that in 1985 about $80 billion in servicing rights changed hands. By 1988, this figure had almost doubled to $150 billion, and given the current state of the industry, increases are likely to continue.

**Total servicing income rose by 8 percent to $211.44 per loan in 1988 as compared with $195.81 per loan in the previous year.**

This increase in servicing transfers reflects ongoing structural changes taking place within the industry. Increased specialization has led many firms to sell their originations servicing released, and others to become exclusively servicers. Consequently, transfers of servicing rights are becoming a standard part of the servicing operation at many institutions. Sales of servicing can be used to generate additional cash to fund losses associated with problem loans, or pay off long-term debt. Just as important, firms can use sales of servicing to restructure their servicing portfolios, in order to obtain an optimum mix between low delinquency and high average loan balance loans. Finally, since servicing trades are now occurring in much smaller denominations in some cases as little as $25 million many small and mid-sized companies, who in the past had been shut out of the market by the sheer size of the transfers being negotiated, may now participate.

**TABLE 1**

**Income and Expenses Per Firm (in Thousands)**
**Average Firm, 1986–1988**

| | 1988 | 1987 | 1986 |
|---|---|---|---|
| **Gross Income, Total** | **$24,187** | **$26,066** | **$25,837** |
| Loan Production | 4,529 | 5,712 | 5,059 |
| Warehousing | 8,104 | 8,979 | 9,602 |
| Marketing | 345 | 1,770 | 3,142 |
| Servicing | 11,209 | 9,605 | 8,035 |
| Servicing, Including Sales of Servicing | 14,759 | N/A | N/A |
| **Expenses, Total** | **$23,767** | **$25,880** | **$20,765** |
| Loan Production | 9,593 | 11,023 | 8,222 |
| Warehousing | 5,410 | 6,699 | 6,258 |
| Marketing | 172 | 394 | 313 |
| Servicing | 8,592 | 7,764 | 5,972 |
| **Net Income, Total (Before Tax)** | **$ 420** | **$ 186** | **$ 5,072** |
| Loan Production | (5,064) | (5,311) | (3,163) |
| Warehousing | 2,694 | 2,280 | 3,344 |
| Marketing | 173 | 1,376 | 2,829 |
| Servicing | 2,617 | 1,841 | 2,063 |
| Servicing, Including Sales of Servicing | 6,167 | N/A | N/A |
| **Memorandum Items:** | | | |
| Profit Margin (Before Tax) | 1.7 | 0.7 | 19.6 |
| Profit Margin, Including Sales of Servicing (Before Tax) | 14.3 | N/A | N/A |
| Purchased Production as Percent of Total Production | 31 | 33 | 35 |
| Number of Firms Reporting | 114 | 124 | 124 |

**TABLE 2**

**Servicing Income and Expenses Per Loan Serviced**
**Average Firm, 1986–1988**

| | 1988 | 1987 | 1986 |
|---|---|---|---|
| **INCOME** | | | |
| **Servicing Fees** | **$183.60** | **$177.60** | **$161.12** |
| First Mortgages[1] | 194.01 | 173.92 | 160.65 |
| Other Mortgages | 0.34 | 3.68 | 0.47 |
| Amortization of Excess Servicing | (10.75) | N/A | N/A |
| Net Gain (or Loss) on Sale of REO | (1.96) | (5.08) | (10.49) |
| Other Loan Administration Income | 29.80 | 23.29 | 29.90 |
| Total Servicing Income | $211.44 | $195.81 | $180.53 |
| Net Gain (or Loss) on Sale of Servicing | 66.97 | N/A | N/A |
| Total Servicing Income, Including Net Gain (or Loss) on Sale of Servicing | $278.41 | N/A | N/A |
| **EXPENSES** | | | |
| **Personnel** | **$ 37.63** | **$ 40.84** | **$ 37.63** |
| Loan Administration Employees | 30.44 | 33.56 | 31.25 |
| Management and Directors | 0.68 | 1.11 | 0.21 |
| All Other Personnel | 0.42 | 0.39 | 0.86 |
| Fringe Benefits | 5.94 | 5.63 | 5.08 |
| Education and Training | 0.15 | 0.15 | 0.23 |
| **Occupancy** | **5.67** | **5.38** | **4.58** |
| **Electronic Data Processing** | **8.69** | **10.14** | **9.05** |
| **Other Direct expenses** | **35.56** | **41.46** | **31.66** |
| Expenses to Service Foreclosures and REO | 8.07 | 15.14 | N/A |
| Corporate Interest Losses on MBS Pools | 2.99 | N/A | N/A |
| Equipment Rentals and Depreciation, Excluding EDP | 1.22 | 1.57 | 1.67 |
| All Other Direct Expenses | 23.28 | 24.75 | 29.99 |
| **Total Direct Expenses** | **$ 87.55** | **$ 97.82** | **$ 82.92** |
| **Provision for Loan Losses** | **27.39** | **13.41** | **12.19** |
| **Amortized Cost of Purchased Servicing** | **47.14** | **47.09** | **39.46** |
| **Net Servicing Income (Before Tax)** | **$ 49.36** | **$ 37.49** | **$ 45.96** |
| **Memorandum Items:** | | | |
| Servicing Profit Margin (Before Tax) | 23.3 | 19.1 | 25.5 |
| Servicing Profit Margin, including Net Gain (or Loss) on Sale of Servicing (Before Tax) | 41.8 | N/A | N/A |
| Servicing Income as Percent of Dollar Volume Serviced | 0.451 | 0.428 | 0.438 |
| Servicing Fees as Percent of Dollar Volume Serviced | 0.392 | 0.388 | 0.390 |
| Servicing Expense Ratio[2] | 0.187 | 0.214 | 0.201 |
| Number of Firms Reporting | 114 | 124 | 124 |

[1] 1988 servicing fees on first mortgages represent gross servicing fees. In prior years, they represented servicing fees on first mortgages less amortization of excess servicing. This year amortization of excess servicing is a separate line item. Comparisons can still be made between total servicing fee income.

[2] Total Direct Expenses as a percent of dollar volume serviced.

Given the increased importance of transfers of servicing rights, this year's survey for the first time sought to capture the gains (losses) related to the sales of servicing rights. On a per loan basis, revenues from sales of servicing averaged $66.97 in 1988. Thus, when this short-run stimulant to income is included, net servicing income more than doubles to $116.33 per loan at the average firm. In addition, when including gains from sales of servicing, the profit margin from the servicing operation jumped to 42 percent.

Based on responses to the survey, small firms tend to be net sellers of servicing rights, while large servicers are usually net purchasers. The servicing acquisition ratio (SAR) illustrates this point. The SAR represents the net gain in servicing volume relative to the volume of servicing rights generated through in-house and purchased originations. The SAR for the average firm in 1988 was 1.01, which essentially means that the volume of loans added to the servicing portfolio, approximately equalled the volume of loans originated by the firm. But, for companies with servicing portfolios of less than $1 billion, the SAR was only 0.38, indicating they were net sellers of servicing rights. While for companies with servicing portfolios greater than $4 billion, the SAR was 1.47, signifying that they are net purchasers of servicing rights. (See Table 3).

### Servicing expenses

In 1988, for the first time in five years, total servicing costs remained essentially unchanged. On a per loan basis, total servicing expenses were $162.08 in 1988, as compared to $158.32 in 1987, an increase of only 2 percent. This stability contrasts sharply with the average for the 1980-1987 period, when total servicing expenses rose about 17 percent per year.

Servicing costs can be broken down into three broad areas; direct expenses, provision for loan losses, and the amortized cost of purchased servicing (ACPS). In 1988, direct expenses declined by 10½ percent, and the ACPS was unchanged. But, these were offset by a twofold increase in provision for loan losses.

Direct expenses fell to $87.55 per loan in 1988. As a percent of dollar

volume serviced, direct expenses declined to 19 basis points, 2 basis points below the 1987 level, and 1 basis point lower than in 1986. This decline is welcome news, and indicates that the concerted efforts of servicing managers to contain the basic costs related to servicing are bearing fruit.

Within direct expenses, personnel costs, which account for about 40 percent of direct expenses, declined for the first time since 1984. On a per loan basis, personnel expenses fell by 8 percent in 1988 to $37.63, from $40.84 in the prior year. Combining this drop with the rise in servicing volume means that as a percent of dollar volume serviced, personnel costs were only 8 basis points in 1988, the lowest they have been in the 1980s. (See Table 4).

The reduction in personnel costs reflects both a small rise in salaries for loan administration employees and staff cutbacks. Average salaries for servicing employees increased only 3.6 percent in 1988 to $18,978. This follows much larger increases of 9 percent and 10 percent in the previous two years. But also important was the drop in employment. At the average firm, the number of loan administration employees fell by 4 percent, to 88 employees.

Occupancy expenses did go up by 5.4 percent in 1988, to $5.67 per loan. However, the size of this increase compares quite favorably with the substantial increases recorded in 1986 and 1987, when occupancy expenses rose 17 percent and 25 percent, respectively. Moreover, given the rise in servicing volume, occupancy expenses as a percent of dollar volume serviced remained unchanged at 12 basis points.

In another key area of direct expenses, electronic data processing (EDP) costs per loan reversed their upward trend, falling for the first time in five years. In 1988, EDP expenses per loan declined 14 percent to $8.69. This drop may be the result of the slowdown in mortgage loan prepayments. Heavy prepayment activity, such as occurred in 1986 and 1987, requires an abnormally large number of computer inquiries, that are costly and can push up EDP expenses. With the drop in loan refinancings in 1988, computer usage may have returned to more normal levels. But it also might reflect the increased use of more cost-effective technologies including optical disks for data management, power dialing and computer voice response systems to increase operating efficiency.

Finally, other direct expenses fell about 14 percent to $35.56 per loan. This drop mainly reflects a decline in expenses to service foreclosures and REO. Other components of this category also declined modestly.

As expected given the increases in sales of servicing, the ACPS component of expenses has jumped to a new level in the past few years. In 1980, the ACPS represented only 19 percent

**TABLE 3**

**1988 Servicing Income and Expenses per Loan Serviced Grouped by Dollar Volume of Loans Serviced**

| | Less than $500 Million | $500 Million to $999 Million | $1 Billion to $3.99 Billion | $4 Billion or More | Average Firm |
|---|---|---|---|---|---|
| **INCOME** | | | | | |
| **Servicing Fees** | **214.91** | **$202.14** | **$188.08** | **$178.84** | **$183.60** |
| First Mortgages[1] | 221.70 | 226.43 | 200.48 | 187.28 | 194.01 |
| Other Mortgages | 0.94 | 0.13 | 1.11 | 0.01 | 0.34 |
| Amortization of Excess Servicing | (7.73) | (24.42) | (13.51) | (8.45) | (10.75) |
| **Net Gain (or Loss) on Sale of REO** | **(4.89)** | **(4.09)** | **(4.07)** | **(0.74)** | **(1.96)** |
| **Other Loan Administration Income** | **27.91** | **28.63** | **27.56** | **30.95** | **29.80** |
| **Total Servicing Income** | **$237.93** | **$226.68** | **$211.57** | **$209.05** | **$211.44** |
| **Net Gain (or Loss) on Sale of Servicing** | **106.32** | **91.08** | **83.79** | **56.07** | **66.97** |
| **Total Servicing Income, Including Net Gain (or Loss) on Sale of Servicing** | **$344.25** | **$317.76** | **$295.36** | **$265.12** | **$278.41** |
| **EXPENSES** | | | | | |
| **Personnel** | **$ 59.62** | **$ 49.48** | **$ 38.86** | **$ 35.24** | **$ 37.63** |
| Loan Administration Employees | 49.93 | 41.34 | 31.57 | 28.25 | 30.44 |
| Management and Directors | 1.90 | 0.76 | 0.21 | 0.84 | 0.68 |
| All Other Personnel | 0.00 | 0.65 | 1.10 | 0.12 | 0.42 |
| Fringe Benefits | 7.50 | 6.49 | 5.71 | 5.94 | 5.94 |
| Education and Training | 0.29 | 0.24 | 0.27 | 0.09 | 0.15 |
| **Occupancy** | **8.58** | **8.08** | **5.48** | **5.43** | **5.67** |
| **Electronic Data Processing** | **11.40** | **12.40** | **8.63** | **8.28** | **8.69** |
| **Other Direct Expenses** | **37.80** | **46.00** | **31.11** | **36.47** | **35.56** |
| Expenses to Service Foreclosures and REO | 6.29 | 10.13 | 5.99 | 8.85 | 8.07 |
| Corporate Interest Losses on MBS Pools | 1.13 | 6.36 | 3.37 | 2.59 | 2.99 |
| Equipment Rentals and Depreciation, Excluding EDP | 1.87 | 2.22 | 1.40 | 1.03 | 1.22 |
| All Other Direct Expenses | 28.51 | 27.29 | 20.35 | 24.00 | 23.28 |
| **Total Direct Expenses** | **$117.40** | **$115.96** | **$ 84.08** | **$ 85.82** | **$ 87.55** |
| **Provision for Loan Losses** | **3.60** | **15.72** | **9.66** | **36.99** | **27.39** |
| **Amortized Cost of Purchased Servicing** | **24.23** | **26.93** | **33.21** | **55.83** | **47.14** |
| **Net Servicing Income (Before Tax)** | **$ 92.70** | **$ 68.07** | **$ 84.62** | **$ 30.81** | **$ 49.36** |
| **Memorandum Items:** | | | | | |
| Servicing Fee (%) | 0.419 | 0.421 | 0.394 | 0.387 | 0.392 |
| Number of Loans Serviced per Servicing Employee | 415 | 459 | 626 | 644 | 616 |
| Average Loan Size Serviced | $51,260 | $48,059 | $47,700 | $46,231 | $46,863 |
| Average Number of Loans Serviced | 4,086 | 15,145 | 44,125 | 215,266 | 53,008 |
| Average Dollar Volume of Servicing (Millions) | $ 209 | $ 728 | $ 2,105 | $ 9,952 | $ 2,484 |
| Percent Growth, Dollar Volume of Servicing | 13.4 | 6.9 | 6.1 | 15.7 | 12.4 |
| Servicing Acquisition Ratio | 0.473 | 0.236 | 0.761 | 1.474 | 1.008 |
| Number of Firms Reporting | 35 | 23 | 38 | 18 | 114 |

[1] 1988 servicing fees on first mortgages represent gross servicing fees. In prior years, they represented servicing fees on first mortgages less amortization of excess servicing. This year amortization of excess servicing is a separate line item. Comparisons can still be made between total servicing fee income.

of total costs, by 1988 it had increased to 29 percent. On a per loan basis, the ACPS was $47.14 in 1988, essentially the same as in 1987, but still almost three times as much as the 1980-1985 average. Lower mortgage prepayments in 1988 may have helped to hold down the ACPS component of expenses, because the unamortized portion of the costs of purchased servicing must be written off as expenses when loans are removed from the books through repayment.

The servicing operation continued to be plagued by heavy losses related to delinquency and foreclosure problems in 1988. In 1988, total expenses for problem loans which includes provision for loan losses, losses on sales of REO, and expenses to service foreclosures and REO was $37.42 per loan, 11 percent higher than the $33.63 figure recorded in the prior year. All of the increase was in provision for loan losses, which more than doubled, rising to $27.39 per loan in 1988, from $13.41 per loan in 1987. Provision for loan losses in 1988 represented 17 percent of total servicing expenses; in 1980, they accounted for only 1 percent of total costs. The other two costs associated with problem loans improved in 1988. Losses from sales of REO were only ($1.96) per loan in 1988 as compared with ($5.08) per loan in the prior year. Furthermore, expenses to maintain foreclosed properties was nearly cut in half, dropping to $8.07 per loan in 1988 from $15.14 per loan in 1987. (See Table 5).

Heavy use of the no-bid option on VA foreclosures continued to be a major factor in foreclosure costs. During 1988, VA foreclosures rose another 10 percent to 47,712 loans, and no-bids represented a higher proportion of the total. The no-bid option was utilized in 24 percent of the VA foreclosures in 1988 as compared with 21 percent in 1987. Given that losses from a no-bid foreclosure were between $15,000 to $20,000, this trend is critical to mortgage bankers, who service an estimated 70-75 percent of all VA loans. Fortunately, evidence from other sources indicates that the no-bid situation stabilized in 1989.

As in past years, economies of scale continued to be evident in 1988, with the larger firms tending to have both higher levels of productivity and lower direct costs. For instance, at firms with servicing portfolios of less than 5,000 loans, the number of loans serviced per servicing employee was only 366, while at firms with servicing portfolios greater than 70,000 loans, the number of loans serviced per servicing employee was 644. Further support for this view can be found by comparing the most productive servicers with their less efficient competitors. At companies where the number of loans serviced per servicing employee was greater than 700, the average dollar volume serviced was $4.7 billion. In contrast, at firms with less than 400 loans serviced per servicing employee, servicing volume averaged only $480 million.

As expected, these differences in productivity dramatically affect direct costs, with the most efficient servicers having the lowest direct costs on a per

**TABLE 4**

**Miscellaneous Servicing Expenses**

| | 1988 | 1987 | 1986 | 1985 |
|---|---|---|---|---|
| **Personnel Expenses, 1985–1988** | | | | |
| Number of Loans Serviced per Servicing Employee | 616 | 570 | 549 | 579 |
| Average Salary Loan Administration Personnel | $18,978 | $18,324 | $16,774 | $15,187 |
| Total Personnel Expenses per Loan Serviced | $ 37.64 | $ 40.84 | $ 37.62 | $ 33.58 |
| Personnel Expense as a Percent Dollar Volume Serviced | 0.080 | 0.089 | 0.091 | 0.090 |
| Personnel Expense as a Percent of Total Direct Servicing Expense | 43 | 42 | 45 | 51 |
| **Other Expenses, 1985–1988** | | | | |
| Occupancy Expenses per Loan Serviced | $ 5.67 | $ 5.38 | $ 4.58 | $ 3.68 |
| Occupancy Expenses per Loan Administration Employee | $ 3,487 | $ 2,905 | $ 2,393 | $ 2,053 |
| Occupancy as a Percent of Dollar Volume Serviced | 0.012 | 0.012 | 0.011 | 0.010 |
| EDP Expense per Loan Serviced | $ 8.69 | $ 10.14 | $ 9.05 | $ 6.68 |
| EDP Expense per Loan Administration Employee | $ 5,342 | $ 5,473 | $ 4,727 | $ 3,747 |
| EDP Expense as a Percent of Dollar Volume Serviced | 0.019 | 0.022 | 0.022 | 0.018 |
| Other Direct Expenses per Loan Serviced | $ 35.56 | $ 41.46 | $ 31.65 | $ 22.11 |
| Other Direct Expenses as a Percent of Dollar Volume Serviced | 0.076 | 0.091 | 0.077 | 0.059 |

**TABLE 5**

**Trends in Servicing Costs**
**Average Firm, 1979- 1988**

| | 1979 | 1980 | 1981 | 1982 | 1983 | 1984 | 1985 | 1986 | 1987 | 1988 |
|---|---|---|---|---|---|---|---|---|---|---|
| **Selected Expenses per Loan:** | | | | | | | | | | |
| Provision for Loan Losses | $0.29 | $ 0.48 | $ 0.86 | $ (0.09) | $ 2.43 | $ 4.20 | $ 4.98 | $12.19 | $13.41 | $27.39 |
| Net Losses on Foreclosures | $0.28 | $ 0.16 | $ 0.92 | $ 1.11 | $ 1.75 | $ 4.99 | $ 6.77 | $10.49 | $ 5.08 | $ 1.96 |
| Amortized Cost of Purchased Servicing | $6.25 | $10.25 | $10.58 | $15.03 | $17.88 | $20.15 | $23.88 | $39.46 | $47.09 | $47.14 |
| Expenses to Service Foreclosures and REO | N/A | N/A | N/A | N/A | N/A | N/A | N/A | N/A | $15.14 | $ 8.07 |

# —THE— QUALIFIER —SERIES—

*FHA • VA • Conventional*
*Purchase • Refinance*
*Save Time & Avoid Mistakes*
*Submit & Close Loans Faster*
*Look & Be Professional*

## "QUALIFIER"

- *Prequalify Borrowers*
- *Prepare Good Faith Estimates*
- *Compute Borrower's Qualifications, Cash to Close, Ratios, Residual*
- *Computes Federal & State Income Taxes, Social Security/Retirement, Heat, Utilities, Maintenance*
- *Prepares New ARM Disclosure*
- *Prepares Initial Truth in Lending Disclosure (APR)*
- *Seller's Net Work Sheet*
- *Tracking Reports*
- *$167*

***With 1 Year's Upgrades: Only $197***

## "APPTAKER"

*Process & Print:*

- *Application (1003)*
- *Application (2900) (FHA & VA)*
- *Verification(s) of Employment*
- *Verification(s) of Deposit*
- *Mortgage Rating Letter(s)*
- *Landlord Rating Letter*
- *Schedule of Real Estate*
- *Verification of VA Benefits*
- *Transmittal Summary (Conv.)*
- *Mortgage Credit Analysis (FHA)*
- *Loan Analysis (VA)*
- *$367*

***With 1 Year's Upgrades: Only $437***

*Save $107!*

***Buy Both Only $527***

# Byte Enterprises

## (206) 485-9682

*Visa, Mastercard • Easy to Use*
*Menu Driven • New Step By Step Manual*
*Req: IBM/Comp., 640K, DOS 2.10 or later*
*Byte Enterprises, Inc. P.O. Box 82403*
*Kenmore, WA 98028*


**TABLE 6**

**Servicing Income and Expenses per Loan Serviced**
**Ten High-Profit Firms, 1987–1988**

| | 1988 | 1987 |
|---|---|---|
| **INCOME** | | |
| Servicing Fees | $195.06 | $173.91 |
| Net Gain (or Loss) on Sale of Reo | (1.29) | (1.53) |
| Other Loan Administration Income | 25.22 | 24.16 |
| Total Servicing Income | $218.99 | $196.54 |
| Net Gain (or Loss) on Sale of Servicing | 26.44 | N/A |
| Total Servicing Income, Including Net Gain (or Loss) on Sale of Servicing | $245.43 | N/A |
| **EXPENSES** | | |
| Personnel | $ 32.26 | $ 32.08 |
| Occupancy | 3.65 | 2.72 |
| Electronic Data Processing | 5.71 | 4.78 |
| Other Direct Expenses | 23.41 | 20.79 |
| Total Direct Expenses | $ 65.03 | $ 60.37 |
| Provision for Loan Losses | 0.23 | 0.41 |
| Amortized Cost of Purchased Servicing | 4.59 | 2.51 |
| Net Servicing Income (Before Tax) | $149.04 | $133.25 |

loan basis. At firms with at least 700 loans serviced per servicing employee, direct costs per loan were only $63.33. Conversely, at firms with less than 400 loans serviced per servicing employee, direct costs per loan were $160.46.

Finally, in servicing, as in other areas of mortgage banking, some firms tend to outperform the rest. An examination of the 10 most profitable repeat reporters reveals that, in servicing, the key distinction between them and the other survey respondents was their substantially lower expense figures. Total servicing income was quite similar. At $218.99 per loan, servicing income for this group of 10 companies was only 4 percent higher than at the average firm.

> In 1988, for the first time in five years, total servicing costs remained essentially unchanged.

On the other hand, total servicing expenses for these 10 companies were $69.95 per loan, less than half of what they were at the average firm. All three of the broad cost areas were significantly lower for the high profit firms. Direct expenses were only $65.03 per loan, 26 percent less than at the average firm. Higher levels of productivity accounted for much of the difference. For the high profit firms, the number of loans serviced per servicing employee was 703, 14 percent higher than at the average firm. But even more important was the fact that the servicing portfolios for these 10 firms were composed of very high quality loans. Conse- quently, problem loan expenses were just $3.52 per loan, or only 5 percent of their total costs. At the average firm, problem loan expenses were $37.42 per loan, which represented 23 percent of costs. Finally, these 10 firms were not actively involved in the buying or selling of servicing rights. Thus, the ACPS component of expenses as well as the gains from sales of servicing were extremely low. As a result of these cost advantages, net servicing income for these 10 high profit firms was $149.04 per loan, three times higher than at the average firm. (See Table 6). **MB**

*Robert Rosenblatt is an economist with the Mortgage Bankers Association of America.*

# VITAL STATISTICS

## INTEREST RATES & YIELDS
### 1- TO 4-FAMILY MORTGAGES

| | FHA OPINION SURVEY | FHLBB | | | FNMA | | FHLMC | |
|---|---|---|---|---|---|---|---|---|
| 1989 | FHA New Homes[1] | CONVENTIONAL[2] FRM | ARM | Median Cost of Funds FSLIC Institutions | 1-Yr. ARM | FRM Conv. | ARMs | FRMs |
| SEP | 9.95% | 10.35% | 9.62% | 8.07% | 8.49% | 10.03% | 8.71% | 10.13% |
| OCT | 9.84 | 10.37 | 9.52 | 8.01 | 8.30 | 9.81 | 8.62 | 9.95 |
| NOV | 9.71 | 10.36 | 9.39 | NA | 8.13 | 9.67 | 8.51 | 9.77 |
| **DEC** | **NA** | **NA** | **NA** | **NA** | **8.00** | **9.67** | **NA** | **NA** |

## SELECTED SECURITIES

| | | PRIME COMMERCIAL PAPER | U.S. GOVERNMENT | | | | |
|---|---|---|---|---|---|---|---|
| 1989 | FEDERAL FUNDS RATE | (3-Month) | 6-Month | 1-Year | 3-Year | 10-Year | A-Rated Utility |
| SEP | 9.02% | 8.70% | 7.74% | 8.22% | 8.26% | 8.19% | 9.55% |
| OCT | 8.84 | 8.53 | 7.62 | 7.99 | 8.02 | 8.01 | 9.39 |
| NOV | 8.55 | 8.35 | 7.49 | 7.77 | 7.80 | 7.87 | 9.28 |
| **DEC** | **8.45** | **8.29** | **7.42** | **7.72** | **7.77** | **7.84** | **9.36** |

## CURRENT SECONDARY MARKET YIELDS

| 1989 | GNMA[3] | FNMA[3] | FHLMC[3] |
|---|---|---|---|
| SEP | 9.52% | 9.54% | 9.53% |
| OCT | 9.40 | 9.42 | 9.42 |
| NOV | 9.26 | 9.31 | 9.31 |
| **DEC** | **9.26%** | **9.34%** | **9.32%** |

## SPREADS
(Basis Points)

| | GNMA | FNMA | FHLMC |
|---|---|---|---|
| 1989 | Minus 10-Yr. Govt. | Minus 10-Yr. Govt. | Minus 10-Yr. Govt. |
| SEP | 133 | 135 | 134 |
| OCT | 139 | 141 | 141 |
| NOV | 139 | 144 | 144 |
| **DEC** | **142** | **150** | **148** |

## SECONDARY MARKET ACTIVITY
(Dollars in Millions)

| | FNMA | | | | FHLMC | | | | GNMA | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Portfolio | | Mortgage-Backed Securities | | | | | | Pass-Through Securities | |
| 1989 | Commitments | Purchases | Outstanding | Issued | Commitments To Sell | Commitments To Buy | Mortgages Purchased | PCs Issued | Applications | Issued |
| JUL | $2,513 | $2,091 | $200,468 | $5,464 | $5,934 | $6,608 | $5,720 | $5,180 | $4,395 | $4,895 |
| AUG | 2,842 | 2,724 | 203,923 | 5,081 | 7,852 | 5,705 | 7,283 | 8,650 | 6,161 | 5,463 |
| SEP | 2,328 | 2,223 | 208,894 | 6,883 | 7,979 | 7,708 | 7,889 | 8,050 | 5,181 | 5,740 |
| **OCT** | **2,963** | **2,267** | **213,482** | **6,614** | **9,148** | **7,555** | **7,884** | **7,058** | **5,387** | **5,583** |
| 1988 TOTAL | 23,435 | 23,110 | --- | 54,878 | 41,271 | 70,669 | 44,075 | 39,777 | 58,578 | 56,531 |
| 1987 TOTAL | 25,415 | 20,531 | --- | 63,230 | 68,210 | 76,615 | 76,840 | 75,018 | 116,611 | 96,983 |
| 10 MONTH AVG. 1989 | 2,238 | 1,716 | --- | 5,091 | 6,721 | 6,750 | 6,221 | 5,786 | 4,481 | 4,639 |
| 1988 | 2,080 | 1,979 | --- | 4,404 | 3,162 | 5,341 | 3,412 | 3,004 | 4,848 | 4,779 |
| 1987 | 1,940 | 1,549 | --- | 5,415 | 6,368 | 7,272 | 7,060 | 6,908 | 10,834 | 8,760 |

# HOUSING ACTIVITY

## RESIDENTIAL STRUCTURES

(Units in Thousands, Seasonally Adjusted Annual Rates)

| | BY TYPE OF UNIT | | | | | | BY REGION | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | HOUSING STARTS | | | BUILDING PERMITS | | | HOUSING STARTS | | | | BUILDING PERMITS | | | |
| 1989 | Total | 1-4 Units | 5+ Units | Total | 1-4 Units | 5+ Units | Northeast | Midwest | South | West | Northeast | Midwest | South | West |
| AUG | 1,329 | 1,046 | 283 | 1,328 | 1,004 | 324 | 140 | 236 | 563 | 390 | 174 | 263 | 517 | 374 |
| SEP | 1,264 | 1,028 | 236 | 1,319 | 1,012 | 307 | 161 | 248 | 486 | 369 | 170 | 254 | 509 | 386 |
| OCT | 1,428 | 1,085 | 343 | 1,356 | 1,025 | 331 | 180 | 294 | 558 | 396 | 172 | 276 | 492 | 416 |
| **NOV** | **1,361** | **1,066** | **295** | **1,333** | **1,039** | **294** | **186** | **305** | **495** | **375** | **171** | **276** | **487** | **399** |
| 1988 TOTAL | 1,488 | 1,140 | 348 | 1,456 | 1,070 | 386 | 235 | 274 | 575 | 404 | 230 | 266 | 544 | 416 |
| 1987 TOTAL | 1,621 | 1,212 | 409 | 1,535 | 1,114 | 421 | 269 | 298 | 634 | 420 | 272 | 282 | 575 | 406 |
| 11 MONTH AVG. (SAAR) | | | | | | | | | | | | | | |
| 1989 | 1,401 | 1,076 | 325 | 1,339 | 1,013 | 326 | 189 | 274 | 545 | 393 | 184 | 260 | 505 | 390 |
| 1988 | 1,487 | 1,142 | 345 | 1,448 | 1,066 | 382 | 246 | 267 | 571 | 403 | 234 | 259 | 541 | 414 |
| 1987 | 1,656 | 1,234 | 422 | 1,559 | 1,128 | 431 | 276 | 314 | 638 | 428 | 276 | 294 | 581 | 409 |

## HOME SALES

(Units in Thousands)

| | EXISTING HOMES | | | NEW HOMES | | |
|---|---|---|---|---|---|---|
| 1989 | Sold (SAAR) | Available for Sale | Months Supply At Current Sales Rate | Sold (SAAR) | Available for Sale | Months Supply At Current Sales Rate |
| AUG | 3,480 | 2,330 | 8.0 | 723 | 364 | 6.3 |
| SEP | 3,520 | 2,320 | 7.9 | 642 | 366 | 7.2 |
| OCT | 3,480 | 2,170 | 7.5 | 648 | 366 | 6.9 |
| **NOV** | **3,590** | **2,420** | **8.1** | **710** | **365** | **6.3** |
| 1988 TOTAL | 3,594 | --- | --- | 676 | --- | --- |
| 1987 TOTAL | 3,526 | --- | --- | 671 | --- | --- |
| 11 MONTH AVG. (SAAR) | | | | | | |
| 1989 | 3,436 | --- | --- | 659 | --- | --- |
| 1988 | 3,565 | --- | --- | 677 | --- | --- |
| 1987 | 3,544 | --- | --- | 679 | --- | --- |

## VALUE OF NEW PRIVATE CONSTRUCTION PUT IN PLACE

(Units in Billions of 1982 Dollars, Seasonally Adjusted Annual Rates)

| Total[5] | 1-Unit | 2+ Units | Nonresidential |
|---|---|---|---|
| $276.3 | $95.3 | $19.6 | $83.2 |
| 274.5 | 94.2 | 19.0 | 83.0 |
| 274.5 | 94.9 | 18.1 | 83.0 |
| **274.1** | **96.2** | **19.0** | **82.3** |
| 281.8 | 103.5 | 19.3 | 77.9 |
| 283.0 | 100.7 | 22.4 | 78.2 |
| 278.3 | 98.7 | 19.7 | 81.3 |
| 280.3 | 103.3 | 19.3 | 77.6 |
| 282.4 | 100.3 | 22.5 | 77.9 |

# LENDER ACTIVITY

## LONG-TERM MORTGAGE LOANS CLOSED
### By Type of Institution and By Type of Unit
(Dollars in Millions)

| | 1-4 UNITS | | | | | 5+ UNITS | | | | | NONRESIDENTIAL | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Total[a] | Mortgage Bankers | Savings & Loans[1] | Commercial Banks | Life Companies | Total[a] | Mortgage Bankers | Savings & Loans[1] | Commercial Banks | Life Companies | Total[b] | Mortgage Bankers | Savings & Loans[1] | Commercial Banks | Life Companies |
| 1989 | | | | | | | | | | | | | | | |
| JUN | $29,396 | $5,477 | $11,984 | $11,445 | $76 | $2,471 | $159 | $962 | $881 | $163 | $13,150 | $95 | $1,209 | $9,627 | $2,102 |
| JUL | 25,881 | 5,522 | 10,452 | 9,365 | 200 | 1,789 | 296 | 635 | 508 | 222 | 17,345 | 135 | 791 | 14,325 | 1,967 |
| AUG | 31,614 | 6,150 | 13,215 | 11,752 | 113 | 2,580 | 329 | 870 | 1,033 | 223 | 13,884 | 269 | 971 | 10,670 | 1,913 |
| **SEP** | **31,406** | **5,592** | **12,708** | **12,529** | **114** | **2,393** | **678** | **772** | **534** | **229** | **11,254** | **226** | **815** | **8,210** | **1,805** |
| 1988 | | | | | | | | | | | | | | | |
| TOTAL | 374,401 | 85,307 | 186,237 | 95,474 | 3,190 | 37,876 | 4,526 | 20,379 | 6,988 | 3,553 | 175,754 | 1,032 | 22,953 | 119,942 | 29,714 |
| 1987 | | | | | | | | | | | | | | | |
| TOTAL | 449,544 | 110,083 | 208,054 | 124,551 | 3,209 | 44,981 | 2,409 | 22,492 | 8,269 | 3,547 | 168,652 | 2,871 | 25,613 | 110,490 | 28,160 |
| 9 MONTH AVG. | | | | | | | | | | | | | | | |
| 1989 | 28,174 | 5,483 | 12,352 | 9,841 | 99 | 2,444 | 325 | 1,066 | 647 | 191 | 12,324 | 139 | 1,224 | 9,062 | 1,767 |
| 1988 | 31,541 | 7,461 | 15,451 | 8,036 | 244 | 3,031 | 355 | 1,642 | 569 | 298 | 14,327 | 78 | 1,894 | 10,146 | 2,009 |
| 1987 | 40,136 | 10,138 | 18,148 | 11,268 | 295 | 3,949 | 198 | 1,865 | 744 | 275 | 13,160 | 277 | 2,058 | 8,684 | 2,032 |

## MORTGAGE INSURANCE
(Units in Thousands, Dollars in Millions)

| | APPLICATIONS RECEIVED (Units) | | | | LOANS INSURED | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | TOTAL | FHA[a] | VA | PRIVATE | TOTAL | | FHA | | VA | | PRIVATE | |
| | | | | | Units | Amount | Units | Amount | Units | Amount | Units | Amount |
| 1989 | | | | | | | | | | | | |
| AUG | 177 | 110 | 18 | 49 | 105 | $8,208 | 55 | $3,511 | 14 | $1,102 | 35 | $3,595 |
| SEP | 147 | 85 | 16 | 46 | 116 | 8,981 | 68 | 4,326 | 13 | 1,033 | 35 | 3,622 |
| OCT | 151 | 86 | 19 | 46 | 126 | 9,619 | 75 | 4,790 | 16 | 1,217 | 35 | 3,612 |
| **NOV** | **136** | **78** | **18** | **40** | **131** | **9,936** | **82** | **5,240** | **17** | **1,326** | **32** | **3,370** |
| 1988 TOTAL | 1,755 | 949 | 211 | 595 | 1,334 | 98,012 | 699 | 42,577 | 211 | 15,771 | 424 | 39,664 |
| 1987 TOTAL | 2,340 | 1,211 | 408 | 721 | 2,282 | 159,668 | 1,320 | 81,881 | 451 | 33,312 | 511 | 44,475 |
| 11 MONTH AVG. | | | | | | | | | | | | |
| 1989 | 142 | 84 | 16 | 42 | 106 | 8,091 | 61 | 3,842 | 15 | 1,168 | 30 | 3,081 |
| 1988 | 148 | 81 | 17 | 50 | 112 | 8,196 | 58 | 3,552 | 18 | 1,309 | 36 | 3,335 |
| 1987 | 204 | 106 | 36 | 62 | 203 | 14,179 | 114 | 7,381 | 39 | 2,891 | 43 | 3,761 |

NA—Not Available, SAAR—Seasonally Adjusted Annual Rate

[1]Secondary market gross yields. Numbers shown for each month are the average of yields from the first day of the month shown and the first day of the subsequent month.

[2]Effective rate on loans closed.

[3]Securities for 0- to 30-day delivery.

[4]In addition to the categories of private construction shown, the total also includes these categories: residential improvements, railroads, electric light and power, gas, telephone and telegraph, petroleum pipelines, and farm nonresidential.

[5]In addition to the categories shown, the total also includes private pension funds, private MBS conduits, state and local retirement funds, federal credit agencies, mortgage pools, and state and local investment agencies.

[6]Savings & Loans and Mutual Savings Banks.

[7]FHA applications received includes the Direct Endorsement Program.